

**BELLSOUTH**

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March 20, 1995

Mr. William F. Caton  
Acting Secretary  
Federal Communications Commission  
1919 M Street NW - Room 222  
Washington, D.C. 20554

**RECEIVED**

**MAR 23 1995**

**FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY**

RE: CC Docket No. 94-1

Dear Mr. Caton:

Attached is a letter which I sent to Kathleen Wallman of the Common Carrier Bureau today in connection with the above referenced proceeding.

Please call me if you have any questions.

Very truly,



W. W. Jordan  
Executive Director - Federal Regulatory

Attachment

cc: Karen Brinkmann  
Pete Belvin  
Jim Coltharp  
Jim Casserly  
Richard Welch  
Michael Katz  
Kathleen Wallman

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List A B C D E

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Mrs. Kathleen Wallman  
Chief - Common Carrier Bureau  
Federal Communications Commission  
1919 M Street N.W., Room 500  
Washington, D.C. 20554

**FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY**

RE: CC Docket No. 94-1

Dear Mrs. Wallman:

Attached is a chart which analyzes the first year impacts for various alternative adjustments to the LEC price cap plan. Each of these alternatives has been evaluated relative to the current LEC price cap plan and, as can be seen from the results, would significantly reduce shareholder value for the local exchange carriers while significantly improving the shareholder value for the interexchange carriers.

Also attached is a study by PNR and Associates of long distance company call plans. This study uses data collected from long distance telephone bills in 1994. The results of the study indicate that over two third of long distance calls carried by interexchange carriers were billed at tariffed (non-discounted) rates.

The last attachment contains quotes from Wall Street regarding competition in the long distance market; a chart comparing long distance rates and access charges; and a chart comparing the cumulative shareholder returns for long distance carriers relative to the S&P 500 index.

Please call me if you have any questions regarding this data.

Sincerely,



W. W. Jordan  
Executive Director -Federal Regulatory

Attachments

**Projected Impact of Alternative Adjustments to  
LEC Price Cap Plan on LEC and IXC Shareholders**  
(\$ Millions)

	Alternative Adjustment Scenarios		
	2 Percent	4 Percent	6 Percent
<b>LOSSES to LEC SHAREHOLDERS</b>			
Total Access Revenues for Price Cap LECs	21,882	21,882	21,882
x Net Reductions in Revenues from Adjustments to Plan	2.0%	4.0%	6.0%
= Access Revenue Losses	438	875	1,313
x (1-Tax Rate)	0.62	0.62	0.62
= Earnings Reduction	271	543	814
x Current P/E Ratio (market weighted)	15.2	15.2	15.2
= Loss in Shareholder Value	4,124	8,248	12,373
<i>Loss in Shareholder Value as % of Total Market Value of LEC Stocks</i>	<i>2.24%</i>	<i>4.48%</i>	<i>6.72%</i>
<b>GAINS to AT&amp;T and MCI SHAREHOLDERS</b>			
Reductions in Total Access Charges for AT&T and MCI (78% of total reduction in access charges)	342	683	1,024
x (1-Tax Rate)	0.62	0.62	0.62
= Increases in AT&T/MCI Earnings from Access Charge	212	423	635
x Current P/E Ratio for AT&T and MCI (market	16.9	16.9	16.9
= Gain in AT&T/MCI Shareholder Value	3,583	7,140	10,716
<i>Gain in Shareholder Value as % of Total Market Value of AT&amp;T and MCI Stocks</i>	<i>3.80%</i>	<i>7.57%</i>	<i>11.36%</i>
<b>KEY ASSUMPTIONS</b>			
Reductions in Price Cap Index	2%	3%	4%
Increases in Average LEC Productivity Factor	0%	from 3.5% to 4.5%	from 3.5% to 5.5%
AT&T and MCI Combined Market Share	78%	78%	78%
Percent of Access Revenue Reductions Flowed Through to IXC Customers	0%	0%	0%

# **PNR and Associates Bill Harvesting Study**

## *Long Distance Company Call Plans*

### **Introduction**

During the spring and summer of 1994, PNR and Associates, a market research firm headquartered in Philadelphia, PA, collected local telephone, long distance, cable TV and cellular telephone bills from approximately 9,000 households throughout the US. In addition to providing their bills, respondents were asked to complete a brief questionnaire concerning their attitudes towards competition in the telecommunications and cable TV industries. From this information, two databases have been constructed. The *Aggregate Database* contains aggregate bill information for over 8,700 households. The *Call Detail Database* contains call detail information on all long distance calls made by over 6,000 households. Only those households that made long distance calls and provided complete long distance bills were included in the Call Detail database.

### ***Aggregate Database***

The Aggregate Database and associated software provides a quick view of average bill information by customer demographic segment, local exchange provider, long distance carrier, geographic location, etc. In addition, the software containing the database allows an almost instantaneous view of all potential cross-tabulations. For example, the database can be used to examine the average local and long distance bills and associated demographic characteristics of any RBOC's customers that use AT&T as their primary carrier and who are in favor of competition. In addition, the database will provide valuable market intelligence such as estimates of total expenditures on telecommunications services and cable TV by age, income, family size and location of customer.

### ***Call Detail Database***

The Call Detail Database links the aggregate bill information to a customer's call detail information. The database contains information *for each call*. This database can be used to examine the long distance calling characteristics of specific household segments including time-of-day, duration, carrier, type of call (e.g., calling card), call plan (e.g., Friends and Family), and charge per call. Since the database includes the terminating NPA and NXX of each call, it can also be used to quickly determine for any location the percent of toll calling that is interLATA versus intraLATA or to determine the percent of toll calling that terminates outside a local company's serving area as opposed to the toll calling that terminates inside the company's calling area. In addition, valuable market information can be obtained by examining calling patterns such as call concentration in terms of the number of people called or the number of NPA NXXs that are called.

## Long Distance Calling

Of the 8,731 households in the Aggregate database, 7,431 provided long distance bill information including their long distance company. Table 1 summarizes, in quartiles, how much individual households spend on long distance service during a given month.

**Table 1**  
**% Distribution of Monthly Expenditures**

Carrier	less than \$6.24	\$6.24 to \$15.56	\$15.57 to \$32.89	More than \$32.89	Household Count
AT&T	27.75%	25.41%	24.92%	21.92%	4955
MCI	19.39	24.50	25.54	30.57	1253
Sprint	17.88	19.54	25.16	37.42	481
Other	23.99	6.01	23.45	26.55	742
Total					7431

PNR and Associates, Inc. Copyright 1995

## Use of Long Distance Company Call Plans

While the use of long distance company call plans (e.g., "True USA" and "Friends and Family") has grown, the Call Detail database indicates that during 1994, call plans were used by less than one-third of the households in the US and accounted for less than one-third of the total long distance company calls.

Table 2 shows that of the 5,785 households that made long distance calls using an IXC (intraLATA calls made using the local telephone company were not included), 30.8% used a long distance company call plan. Also, Table 2 shows that 32.35% of the long distance calls made were part of a long distance company call plan.

Table 2 shows, for example, that call plans account for 31.58% of *all* residential domestic calls. Not shown in the table, however, is call plan use by each of the major IXCs. The Bill Harvesting study results show that AT&T call plan calls account for 35.88% of all of AT&T's residential domestic MTS calling. Similarly, MCI call plan calls account for 30.47% of MCI's total residential domestic MTS calling, while Sprint call plan calls account for 20.91% of Sprint's residential domestic MTS calling. Slightly more than 50% of international calls were made using call plans.

**Table 2**  
**Long Distance Calling Plans**

	<u>Households</u>	<u>Calls</u>
Domestic Calls	29.08%	31.58%
International Calls	1.30%	0.56%
Other IXC Rate Plans	0.46%	0.21%
<b>Total Rate Plan</b>	<b>30.84%</b>	<b>32.35%</b>
<b>Calls</b>		
<b>Non-Rate Plan Calls</b>	<b>69.16%</b>	<b>67.65%</b>
<b>Total</b>	<b>100.00%</b>	<b>100.00%</b>

PNR and Associates, Inc. Copyright 1995

These results indicate that for this sample of customers, *over two-thirds* of long distance calls carried by the IXCs were billed at non-discount or tariffed rates. PNR and Associates will be conducting a second Bill Harvesting study in the Spring of 1995 in which it will examine changes in calling plan participation as well as other behaviors.

## The View From Wall Street: Competition in the Long Distance Telephone Market

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AT&T and its rivals are pushing some prices up after almost 10 years of steady discounting. This gives AT&T more room to grow profits, and it creates an umbrella over MCI and Sprint, allowing them to raise prices, too.

*(Kenneth Leon, Bear Stearns, 10/20/92)*

AT&T, MCI, and Sprint all have high-quality earnings because they operate in a stable, oligopolistic industry. . . without serious price competition. [T]he only real threat [is] posed by the Regional phone companies which are unlikely to gain regulatory freedom to enter this business for at least 3-5 years. *(Philip A. Managieri, Cowen, 8/23/93)*

Margins improved for all four [long distance] carriers, reflecting an impact from price increases and steady declines in access costs.

*(Daniel P. Reingold and Richard C. Toole, Merrill Lynch, 2/10/94)*

The combination of a cozy oligopoly that wishes to avoid price wars and falling operating expenses primarily due to [exchange] access cost reductions is an unbeatable environment in which to do business. *(Timothy N. Weller and Nick Frelinghuysen, Donaldson, Lufkin & Jenrette, 6/1/94)*

The long distance industry is one of today's premier growth industries. Where else can you find: (1) double-digit unit volume growth, (2) declining unit costs, on a nominal as well as real basis, (3) a \$10 billion barrier to entry, (4) a benign, stable oligopoly where the price leader [AT&T] is looking to generate cash to fund other ventures, and (5) a prohibition on competition. . . It is rare to see a full-fledged price war in an oligopolistic market, witness soft drinks. The same holds true in the long distance market. *(G.W. Woodlief and E. Struminger, Dean Witter, 10/28/94)*

Many investors still seem to believe that there has been some sort of "price war" among the major interexchange carriers. The fact is that although interstate telephone rates have come down by about 50% over the past decade, the entire decline has been "funded" by decreases in the amounts paid by interexchange carriers to the local exchange carriers for "access." *(John Bain, Raymond James & Assoc., 1/12/95)*

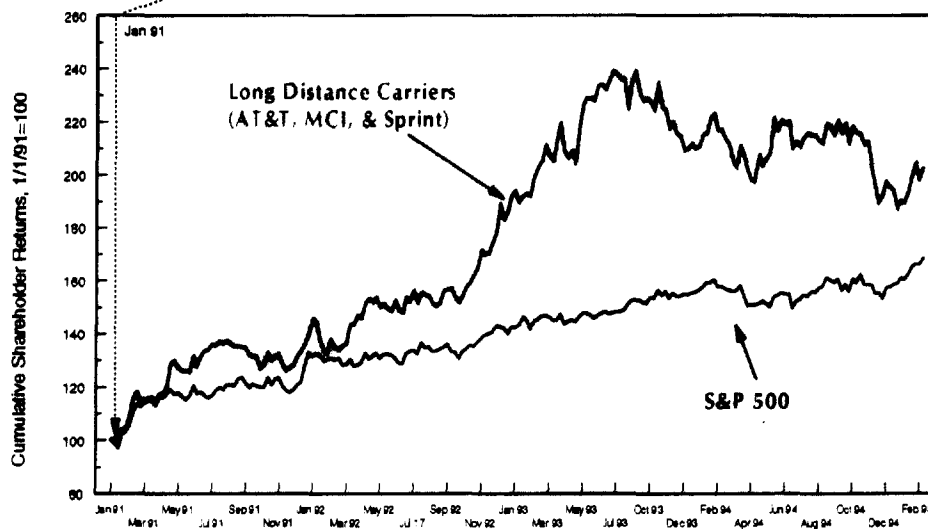
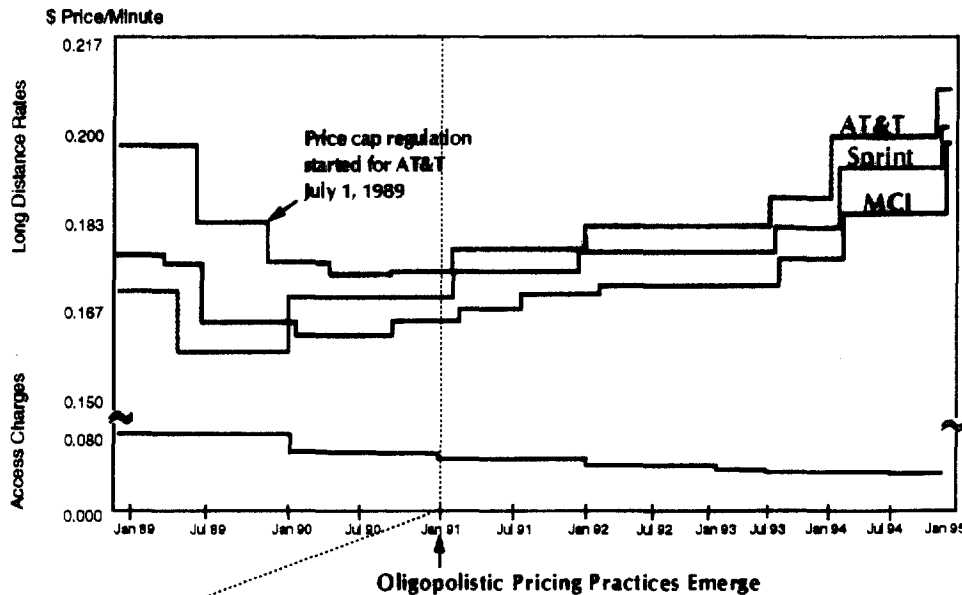
Overall, MCI's new Friends & Family program looks like just another round of discounting funded by previously announced increases in the base rates. By focusing on the discount instead of the rate, the industry has been able to quietly raise base rates while spending millions of dollars promoting ever-increasing discounts. *(D. Reingold and M. Kastan, Merrill Lynch, 1/20/95)*

Regardless of your carrier, you are paying higher and higher rates if you are among the tens of millions of Americans who have not signed up for a discount calling plan. The person paying the retail rate is bearing the disproportionate burden. And these are probably the people who can't afford to make a lot of phone calls and therefore [do not] qualify for those cheaper plans. *(D. Briere, Tele-Choice Inc., 1/21/95)*

AT&T now has the same revenues as the entire Bell system just before the break up in 1984, when they spun off about 85 percent of their assets. *(John Bain, Raymond James & Assoc., 1/24/95)*

MCI. . . filed for a 3.9% across-the-board rate increase. We fully expect AT&T, Sprint, and the second tier carriers to follow suit. This move by MCI is extremely bullish for the long distance stocks since it sends a clear message to the investment community that the long distance industry will practice 'safe pricing' which will lead to stable revenue per minute trends. *(Jack B. Grubman, Salomon Brothers, 2/6/95)*

In fact, a pattern of rising [long distance] prices has emerged in the past year, with a series of AT&T price increases immediately followed by MCI and Sprint price increases. The industry must be careful not to draw the anger of the voting public as the cable industry did before suffering recently at the hands of Congress and the FCC. (*T. Weller and N. Frelinghuysen, Donaldson, Lufkin & Jenrette, 6/1/94*)



The promotions may make it look like there is price competition in residential [long distance markets], but the fact is that the base rates have created profit margins that are much better than you get from [other] businesses. (*H.B. Thompson, LCI International, 9/19/94*)